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No. ———

IN THE
Supreme Court of the United States
OCTOBER TERM, 1983

REPROSYSTEM, B.V., AND N. NORMAN MULLER,
Petitioners,

v.

SCM CORPORATION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTION PRESENTED

Where fraud occurs in the course of face-to-face negotiations for the purchase of securities, must the defrauded party demonstrate the existence of a contract in order to state a cause of action under section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5?

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Petitioners, Reprosystem, B.V.,[1] and N. Norman Muller, respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit entered in this proceeding on February 2, 1984.

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 727 F.2d 257 (2d Cir. 1984) and [1983-1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 99,667 (2d Cir. Feb. 2, 1984) and appears in the Appendix at 1a to 16a. The opinions of the District Court for the Southern District of New York appear in the Appendix at 17a to 89a; three

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[1]Reprosystem, B.V.'s parent company is Reprographex Antilles, N.V. Reprosystem, B.V. has no subsidiaries or affiliates.

of these opinions are reported at 522 F. Supp. 1257 (S.D.N.Y. 1981), 565 F. Supp. 4 (S.D.N.Y. 1982) and [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,207 (S.D.N.Y. June 30, 1981). An unreported judgment of the district court appears in the Appendix at 90a to 91a.

JURISDICTIONAL STATEMENT

The judgment of the Court of Appeals for the Second Circuit was entered on February 2, 1984. On April 19, 1984, Justice Marshall issued an Order extending the time for filing this petition to and including June 2, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) (1982).

STATUTES AND REGULATIONS INVOLVED

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1982), is set forth in the Appendix at 92a. Rule 10b-5, 17 C.F.R. § 240.10b-5 (1983), promulgated thereunder by the Securities and Exchange Commission ("SEC"), is set forth in the Appendix at 92a to 93a.

STATEMENT OF THE CASE

Petitioner Reprosystem, B.V., a Netherlands corporation, was incorporated by petitioner N. Norman Muller and others to purchase the shares and assets of six wholly-owned subsidiaries of respondent SCM Corporation. These six companies ("the companies") were operated by the International Group of SCM's Business Equipment Division and were engaged in the business of marketing, leasing and servicing office copiers, paper and toner throughout Western Europe, the Middle East and Africa.

A. SCM Decides to Sell Shares and Assets of the Companies

Late in 1975 SCM's principal officers, including Paul Elicker, SCM's President, Chief Executive and Chairman

of SCM's Board of Directors, and Herbert Egli, the Vice President-Finance and Controller of SCM, decided to sell the companies primarily because of projections of their decreasing profitability. 522 F. Supp. at 1260, App. at 19a.[2] Mr. Muller learned of this decision through a broker and in April and May 1976 discussed the matter with high-ranking officials of SCM including Mr. Elicker, Frank DeMaio, Vice President and General Manager of SCM's International Group, and William Rodich, President of SCM's Business Equipment Division.

By a letter of May 7, 1976, Mr. Muller offered to pay a total of $9 million for the companies. Mr. Rodich responded that Mr. Muller's letter provided the basis for negotiations, which were held in August and September 1976.

During these negotiations, Mr. Rodich prepared memoranda that contained thirteen points essential to SCM.[3] Mr. Muller agreed to these points and, by mid-September, the parties had reached an agreement in principle on the sale of the companies to Mr. Muller. Under this agreement, as of August 31, 1976, the business was to be operated in its ordinary course by SCM for the account and benefit of Mr. Muller. App. at 22a, 27a.

On September 16, 1976, SCM's Board of Directors approved the agreement in principle and authorized its public announcement. On September 28, 1976, SCM issued a press release which stated that

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[2] This opinion of the district court is reported at 522 F. Supp. 1257 and is reproduced in the Appendix at 17a to 68a. Citations to this opinion in petitioners' statement of facts will be in form "App. at ——."

[3] These memoranda are reproduced in the appendix to the district court's opinion. App. at 67a to 68a.

SCM Corporation has reached an agreement in principle to sell its office copier service organizations in the United Kingdom, France, Germany, Switzerland and Belgium and its distribution operations covering Europe, the Middle East and Africa to a company controlled by N. Norman Muller, a private investor.[4]

App. at 24a. On September 30, 1976, SCM reported the agreement in principle in its Form 10-K filed with the SEC. App. at 24a.

Following the agreement in principle there occurred a period of intense negotiation and drafting. It was understood by all concerned throughout this period that the companies were being operated by SCM for the benefit of Mr. Muller. App. at 29a to 30a. By December 15-16, 1976, 16 drafts of the contract had been produced by SCM's counsel, the New York law firm of Sullivan & Cromwell. A meeting was then held at the request of Mr. Rodich, SCM's principal negotiator, to conclude the discussions. At this meeting two drafts, one a "global" agreement and the other a prototypical agreement for the sale of the shares of one of the companies, were discussed page by page.

At the conclusion of the meeting on December 16 no open terms remained, "[t]he negotiators were released, and adieus, season's greetings and congratulations were exchanged." App. at 32a. Mr. Rodich escorted Mr. Muller to Mr. DeMaio's office and advised Mr. DeMaio that the meeting had been successfully completed. As found by the district court, the import of this meeting of Mr. Rodich, Mr. Muller and Mr. DeMaio was to acknowledge the transfer of power. App. at 32a. Mr. Rodich also took Mr. Muller to Mr. Egli's office and advised Mr. Muller that Mr. Egli would finish up the transaction since Mr. Rodich

[4] This announcement was reported in the New York Times, the Wall Street Journal, and on the Dow Jones ticker tape, among other places.

was about to be reassigned to Baltimore to serve as president of another SCM division.

On December 27, 1976, counsel for SCM provided final copies of the global agreement and the agreements for the purchase of the securities of four of the six companies; shortly thereafter, final documentation for the purchase of the assets of the two remaining companies was furnished by SCM. App. at 35a. As found by the district court, these documents constituted written agreements between the parties on all material terms relating to the sale, and it was so understood by all those involved as of the morning of December 31, 1976. App. at 35a.

B. December 31, 1976—SCM Decides to "Kill the Deal"

On December 31, 1976, Mr. Egli reviewed the final documents relating to the sale. In the course of this review, Mr. Egli began to give serious thought to backing out of the agreement. In notes made at the time, Mr. Egli set forth the "alternatives" he believed were open to SCM, the thrust of which was, as stated in the notes, to "[k]ill [the] deal."[5] Mr. Egli feared that the "deal" which had been struck was, in his words, "good for Muller not good for SCM." App. at 37a.

Mr. Egli discussed these matters with SCM President Elicker and SCM Vice President-Administration Hall on January 4, 1977, discussions which led to the district court's finding that "in January the responsible officers of SCM reached a conclusion to terminate the transaction with Muller." App. at 43a.

C. January-February 1977—SCM Fraudulently Fails to Disclose Its Decision to "Kill the Deal"

Despite the fact that its decision to kill the deal had been made, SCM continued to negotiate—in bad faith—

[5] The alternatives as stated by Mr. Egli in his notes are reproduced in the opinion of the district court. App. at 37a.

with Mr. Muller. SCM raised one new or previously-resolved issue after another, thereby prolonging the negotiations and making it more difficult for Mr. Muller to close the deal. During this period, SCM never disclosed that it had already decided to back out.

SCM began by demanding interest on the purchase price dating back to August 1976, a demand which the district court expressly found to be an "afterthought."[6] App. at 41a. SCM also requested, for the first time, evidence of Mr. Muller's capacity to pay the cash required at closing.

SCM sought a substantial increase in the purchase price and the attendant cash required to close, the latter amount having remained steady at $4.25 million between August and December. This increase was based on: (1) the recalculation by SCM of certain accounts receivable; (2) approximately $145,000 resulting from SCM's demand for interest on the purchase price, and (3) the request by SCM for an additional $540,000 due to an inter-company transfer.[7] SCM also withdrew from its

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[6] At the same meeting Mr. Egli announced his intention to visit the subsidiaries, a trip which the district court found was never satisfactorily explained by Mr. Egli either at the time or at trial. Mr. Egli insisted on making this trip over Mr. Muller's objection that it made more sense to accelerate the paperwork and complete the transaction. App. at 38a to 39a.

As found by the district court, Mr. DeMaio, too, objected to the trip and raised his objection with President Elicker but was overruled. App. at 39a. The district court further found that immediately after Mr. Egli's trip to Europe, Mr. DeMaio was informed by the European managers of the companies that Mr. Egli, during his trip, had indicated serious doubts regarding completion of the transaction. App. at 39a.

[7] The work papers regarding this transfer were never made available to Mr. Muller and the transfer, according to the district court, was never satisfactorily explained by SCM. App. at 40a. Nonetheless, Mr. Muller agreed to all of the price increases demanded by SCM except for the increase representing interest on the purchase price.

previous undertaking not to compete with the companies in the copier field.

SCM also took action inconsistent with the agreement in principle that SCM would operate the companies in the normal course of business and for the benefit of Mr. Muller. Contrary to this understanding, SCM reduced the leasing of new equipment, a mainstay of the companies' business. Mr. Egli single-handedly—and in secrecy—conducted critical negotiations in Europe with a likely supplier of new "plain paper" copying equipment to the companies, having refused Mr. Muller's request to accompany him.[8] Finally, upon Mr. Egli's return from Europe and without warning, Mr. Egli fired Mr. DeMaio—directing that he be escorted out of the building—and also fired the companies' other New York administrators and their secretaries. All of this was done without discussion with Mr. Muller or any prior notice to him, despite the fact that continuity of management had been a requisite of Mr. Muller to which SCM had agreed since early in the negotiations. Although SCM advanced certain reasons for the firing of Mr. DeMaio, the district court found them to be "pretextual, and therefore . . . significant evidence that Egli indeed sought to kill the deal." App. at 42a.

Summarizing the events of January and February 1977, the district court found

> that SCM's financial interest required that the sale not go forward, that Egli realized that fact, that the actions taken in January, 1977 by Egli on behalf of SCM had the effect of slowing down the signing and killing the deal, and that a specific plan for disposi-

[8] Throughout the negotiations with SCM, Mr. Muller had continually advocated the expansion by the companies into "plain paper" copying, which he believed to be essential to the continuation of the companies' business. This expansion, which was resisted by SCM's highest officials, was also favored by SCM managers such as Mr. DeMaio and ultimately proved to be of great financial benefit to the companies.

> tion of each corporation was evolved, contrary to the Agreement in Principle and the Final Drafts.

App. at 43a. However, not until February 4, 1977 did SCM inform Mr. Muller of its decision to "kill the deal". Within a short time after ending talks with Mr. Muller, SCM sold five of the companies individually to other purchasers [9] for profits several million dollars greater than it would have realized if the transaction with Mr. Muller had been completed.

D. Opinions Below

On November 22, 1977, Reprosystem [10] brought this action against SCM, seeking to recover damages arising from, *inter alia*, SCM's breach of contract and its violation of antifraud provisions of the federal securities laws.

In its judgment of June 30, 1981, the district court held that the parties had agreed in December 1976 upon all material terms of a contract for the sale of the shares and assets of the six companies to petitioners. The dis-

[9] On January 20, SCM issued a press release stating that it felt free to pursue "other alternatives" to a sale of the shares and assets of the companies to Mr. Muller. App. at 42a. At least as early as January 25, President Elicker wrote to a potential alternate buyer. (Plaintiff's Exhibit 177)

SCM signed contracts for the sale of five of the companies on the following dates:

United Kingdom	May 6, 1977
Switzerland	May 20, 1977
France	June 22, 1977
Germany	November 3, 1977
Belgium	January 19, 1978

The sixth company was liquidated.

Both the separate disposition of each company and the liquidation of SCM's investment in the companies were alternatives described by Mr. Egli in his notes made at the time of his review on December 31, 1976. *See supra* at 5.

[10] An amended complaint was filed by Reprosystem and Mr. Muller on November 17, 1978.

trict court held that SCM breached the contract as well as its duty of good faith negotiation and performance.[11]

Turning to petitioners' securities fraud claims, the district court ruled that under the "sale of business" doctrine, the federal securities laws did not apply to the sale by SCM of the shares of four of the companies to petitioners.[12] However, the court did expressly take note of SCM's "failure to disclose the fact of a decision to 'kill the deal'" and emphasized its concern that "[w]ere the federal securities laws applicable, this omission would require further analysis." App. at 50a.[13]

On appeal, the court of appeals reversed the district court's holding that a contract existed between the parties. With respect to the securities fraud claims, the court of appeals noted its then-recent rejection of the sale of business doctrine. However, it ruled that because there was no contract between the parties for the purchase of securities, petitioners could not recover for securities fraud.

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[11] The court held that petitioners were entitled to damages as measured by SCM's unjust enrichment from profits received from the companies during the parties' negotiations. In a separate opinion and judgment, the district court awarded petitioners $1.062 million in damages arising out of SCM's breach of contract. 565 F. Supp. 4, App. at 89a, 90a.

[12] Subsequent to the district court's judgment, the Court of Appeals for the Second Circuit rejected the "sale of business" doctrine. *See* Golden v. Garafalo, 678 F.2d 1139 (2d Cir. 1982).

[13] At trial, petitioners alleged that SCM had also fraudulently overstated the assets and the income of the companies during the parties' negotiations. The district court found no fraudulent intent with regard to these misstatements. App. at 50a. Petitioners do not raise these allegations of fraud before this Court.

REASONS FOR GRANTING THE WRIT

I. THE ISSUE RAISED BY THIS PETITION IS RECURRING AND IMPORTANT TO THE INTEGRITY OF NEGOTIATIONS FOR THE PURCHASE OF SECURITIES

The court of appeals grounded its holding that petitioners could not recover damages under the federal securities laws on its conclusion that they "were not and do not claim to be actual purchasers or sellers of SCM stock." 727 F.2d at 265, App. at 15a. Consequently, "they do not satisfy the 'purchase or sale' requirement of *Birnbaum v. Newport Steel*, 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S. 956 (1952)." *Id.*, App. at 15a.

Significantly, the court of appeals did not discuss or cite this Court's decision in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). In *Blue Chip Stamps*, the Court found that offerees of a stock offering made pursuant to an antitrust consent decree did not have standing to maintain a private cause of action for money damages where they had not purchased any of the offered shares. The Court reasoned that, in the context of the public securities markets, this rule was necessary to avoid unlimited liability to an unlimited number of non-purchasing plaintiffs, whose claims would be difficult to disprove.

At the same time, the Court in *Blue Chip Stamps* recognized the existence of a second universe of cases—involving individually negotiated transactions and privity of dealing—where the considerations which led to this holding do not apply.[14] Such cases pose none of the dan-

[14] That such cases were recognized as a separate universe by the *Blue Chip Stamps* majority is also implicit in the fact that this category of cases does not fall into any of the "[t]hree principal classes of potential plaintiffs" which the *Blue Chip Stamps* majority noted were barred from standing by its holding, *viz.*, (1) "potential purchasers of shares, either in a new offering or on

gers, such as an unlimited class of plaintiffs, speculative damages, and "strike" suits, which were of such concern in *Blue Chip Stamps.* Indeed, as the majority in *Blue Chip Stamps* acknowledged, under the common law a contract has never been viewed as a prerequisite to an action for fraud in the context of face-to-face negotiations. *See* 421 U.S. at 744-45.

Through review of this case, this Court can make explicit the logical limits of *Blue Chip Stamps* by holding that where fraud occurs in the course of face-to-face negotiations for the purchase of securities, the defrauded party has standing to sue under section 10(b) and Rule 10b-5.[15] Such a holding will give effect to Congress' desire in enacting the antifraud provisions of the securities laws to prevent fraud in this kind of securities transaction, without fostering vexatious or unfounded litigation.

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the Nation's post-distribution trading markets, who allege that they decided not to purchase because of an unduly gloomy representation or the omission of favorable material which made the issuer appear to be a less favorable investment vehicle than it actually was," (2) "actual shareholders in the issuer who allege that they decided not to sell their shares because of an unduly rosy representation or a failure to disclose unfavorable material," and (3) "shareholders, creditors, and perhaps others related to an issuer who suffered loss in the value of their investment due to corporate or insider activities in connection with the purchase or sale of securities which violate Rule 10b-5." *See* 421 U.S. at 737-38.

[15] As the court of appeals in this case observed, defrauded parties do have standing under the federal securities laws if they have entered into a contract to purchase securities. *See* 727 F.2d at 265, App. at 15a to 16a. *Accord* Threadgill v. Black, [1983-1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 91,402 (D.C. Cir. Mar. 27, 1984).

A. The Reasons for Not Finding Standing to Sue for Fraud in Uncompleted Transactions in the Securities Markets Do Not Exist With Respect to Fraud in Face-to-Face Negotiations for the Purchase of Securities

In *Blue Chip Stamps* the Court recognized that "[t]he *Birnbaum* rule undoubtedly excludes plaintiffs who have in fact been damaged by violations of Rule 10b-5, and to that extent it is undesirable." 421 U.S. at 743. The Court was concerned, however, with the problems of proof inherent in the situation of a nonpurchasing plaintiff; it feared conferring standing upon a limitless class of putative plaintiffs seeking undocumented damages. The Court noted that private actions under Rule 10b-5 provided a singular opportunity for bringing "strike" suits, cases with "settlement value to the plaintiff out of any proportion to [their] prospect of success at trial. . . ." *Id.* at 740. The Court also expressed a fear of "throw[ing] open to the trier of fact many rather hazy issues of historical fact the proof of which depended almost entirely on oral testimony." *Id.* at 743.

While these fears may have been well founded in cases involving fraud in the securities markets, they are not valid in face-to-face negotiations for the purchase of securities. In that context, "strike" suits are unlikely, if not altogether impossible. Parties to such negotiations are known to one another and, indeed, have voluntarily chosen to deal with one another. The number of such cases, and hence the number of potential plaintiffs, is necessarily limited. The purchaser in an individually negotiated transaction does not have the leverage of a potential class action. Most importantly, the correspondence and conduct of the parties over a period of time eliminate the problems of proof and documentation of damages that were of concern in *Blue Chip Stamps*.

Such cases thus do not present the spectre, seen by both the majority and concurring opinions in *Blue Chip Stamps*, of affording standing to a legion of "bystanders to the securities marketing process" waiting on the sidelines for the prices of stocks to rise in order to seek a "largely conjectural and speculative recovery in which the number of shares involved will depend on the plaintiff's subjective hypothesis." *See* 421 U.S. at 735, 747; *id.* at 758-59 (Powell, Stewart & Marshall, JJ., concurring). In short, "the very necessity, or at least the desirability, of fashioning unique rules of corroboration and damages" for open market transactions, *see id.* at 744, is altogether absent in cases involving face-to-face negotiations.[16]

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[16] The majority opinion in *Blue Chip Stamps* also referred to the legislative history of section 10(b) and the language of the statute. Both of these aspects of that opinion deserve further analysis.

The majority in *Blue Chip Stamps* noted the SEC's unsuccessful attempts in 1957 and 1959 to have Congress amend section 10(b) to broaden its coverage. *See* 421 U.S. at 732. This aspect of the legislative history had not been suggested or briefed by any of the parties. The majority opinion apparently relies only upon a memorandum prepared in 1959 by the staff of the Senate subcommittee which simply summarizes the arguments of the SEC in favor of the amendment and the arguments of the securities industry against it. *See* SEC Legislation, Hearings on S. 1178-1182 Before a Subcomm. of the Senate Comm. on Banking & Currency, 86th Cong., 1st Sess., 367-68 (1959).

The broad language of the statute, which provides antifraud coverage "in connection with" purchases or sales of securities, was briefly discussed by the Court. *See* 421 U.S. at 733-34 & n.5. Its narrow reading of the statute, rejected by the *Blue Chip Stamps* dissent, *see id.* at 761-71 (Blackmun, Douglas & Brennan, JJ., dissenting); *see also* Eason v. Gen. Motors Acceptance Corp., 490 F.2d 654 (7th Cir. 1973), *cert. denied*, 416 U.S. 960 (1974) (Stevens, J.), was prompted at least in part by the majority's fear that the broader construction called for by the plain language of the statute might "provide a cause of action, not to purchasers and sellers of securities, but to the world at large." 421 U.S. at 733 n.5. Although this may be a valid concern with respect to

This last point is recognized in *Blue Chip Stamps* itself. Noting that there is "certainly" a relationship between the common law tort of misrepresentation and deceit and a claim of fraud under Rule 10b-5, the Court observed that "it has long been established in the ordinary case of deceit that a misrepresentation which leads to a refusal to purchase or to sell is actionable in just the same way as a misrepresentation which leads to the consummation of a purchase or sale. *Butler v. Watkins*, 13 Wall. 456 (1872)." 421 U.S. at 744. The Court declined to apply this rule, however, because the facts of the case before it were so markedly different from those in which the common law rule evolved.

In support of its comparison, the Court discussed at length the facts of *Butler* in which the plaintiff alleged that defendant had fraudulently professed an intent to enter into an agreement, while having no intention of doing so. Careful note was taken that the parties in *Butler* "met with one another in New Orleans, that one presented a draft agreement to the other, and that letters were exchanged relating to that agreement." *Id.* at 745. The Court further noted that the parties "had concededly been engaged in the course of business dealings with one another, and would presumably have recognized one another on the street had they met." *Id.*

This situation—"the typical fact situation in which the classic tort of misrepresentation and deceit evolved"—was viewed as "light years away" from the stock market transactions with which the Court was concerned in *Blue Chip Stamps*. *Id.* at 744-45. It is, however, precisely the situation in this case. Indeed, far from presenting the danger of a case-by-case erosion of *Blue Chip Stamps*, *see id.* at 755, this case typifies those cases involving face-to-face negotiations factually similar to those in

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transactions in the securities markets, this concern is unfounded in cases typified by the negotiated transaction in which petitioners engaged.

Butler. In view of this similarity, the logic of *Blue Chip Stamps* calls for a finding of standing in this case.[17]

B. Compelling Reasons Exist to Apply Section 10(b) and Rule 10b-5 to Face-to-Face Negotiations for the Purchase of Securities

Apart from the logic of *Blue Chip Stamps*, there are compelling reasons to apply section 10(b) and Rule 10b-5 to face-to-face negotiations for the purchase of securities.

The interest which petitioners seek to vindicate comes within the fundamental congressional purpose in enacting section 10(b), *i.e.*, to require full disclosure in transactions involving securities.[18] The coverage of the antifraud provisions of the securities laws is not limited to instruments traded at securities exchange. Thus, in *Superintendent of Insurance v. Bankers Life & Casualty Co.*, 404 U.S. 6, 10 (1971), this Court held the securities

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[17] The Court in *Blue Chip Stamps* also noted the accumulation of cases applying the *Birnbaum* rule. 421 U.S. at 737. However, as Judge, now Justice, Stevens pointed out in Eason v. Gen. Motors Acceptance Corp., at the time *Birnbaum* was decided, "the rule . . . was thought to relate only to public sales of securities. . . ." 490 F.2d at 658. Thus, neither *Birnbaum* nor its progeny had occasion to address the question whether that rule should be applied to a private, negotiated transaction.

[18] *See, e.g.*, Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 477 (1977). In Affiliated Ute Citizens v. United States, 406 U.S. 128, 151 (1972), this Court stated that Rule 10b-5 prohibits "any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person," and held that the proscriptions under section 10(b) and Rule 10b-5 "are broad and, by repeated use of the word 'any,' are obviously meant to be inclusive." Furthermore, as the Court has repeatedly recognized, Congress intended that the "securities laws combating fraud should be construed 'not technically and restrictively, but flexibly to effectuate [their] remedial purposes.'" Herman & MacLean v. Huddleston, 103 S. Ct. 683, 690 (1983), quoting SEC v. Capital Gains Research Bureau, 375 U.S. 180, 195 (1963); Blue Chip Stamps, 421 U.S. at 748; Affiliated Ute Citizens, 406 U.S. at 151.

laws applicable to a negotiated transaction in securities, stating that section 10(b) applies regardless of whether the transaction is conducted through an organized market. The antifraud provisions have "always been understood to apply to transactions in shares of close as well as publicly held corporations and to negotiated as well as market sales and purchases of shares." *Golden v. Garafalo*, 678 F.2d 1139, 1446-47 (2d Cir. 1982). Indeed, by the very act of "choosing to deal in stock, the parties may have created an expectation, deserving of some consideration, that the securities laws would apply." *Daily v. Morgan*, 701 F.2d 496, 503 (5th Cir. 1983).[19]

The comprehensive protection of the federal securities laws is essential to preserve the integrity of individually negotiated stock transactions. In the context of face-to-face negotiations there are numerous opportunities for misrepresentations to occur, many of which are not present in exchange transactions. Negotiations can be arduous and expensive. Vast amounts of capital may be at risk. These transactions are frequently national or, as in this case, international in scope. Regardless of whether the parties reach a contract, federal securities laws coverage—and concomitant federal jurisdiction—are essential to insure the integrity of the negotiating process.

In fact, there are important reasons supporting a federal private right of action for fraud in a negotiated transaction that are not applicable to transactions in the securities markets. Many federal securities laws, such as

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[19] As Judge, now Justice, Stevens stated in Eason v. Gen. Motors Acceptance Corp., 490 F.2d at 659, "a formal purchaser-seller limitation" in all circumstances is not consistent with the overriding purposes of the 1934 Act. "The emphasis on the injured party's status as an investor indicates that the protection of the rule extends to persons who, in their capacity as investors, suffer significant injury as a direct consequence of fraud in connection with a securities transaction, even though their participation in the transaction did not involve either the purchase or the sale of a security." *Id.*

those requiring the preparation of prospectuses and the filing of registration statements, provide substantial protection to purchasers of stock in securities markets which is often unavailable to those who purchase stock in negotiated transactions. The SEC also plays a far more active policing role in securities markets than it could possibly play in negotiated purchases or sales of stocks.

While execution of a contract is one means of obtaining protection, negotiating parties who fail to achieve a contract have no federal securities law protection against fraud in the negotiation process.[20] Indeed, federal protection is particularly necessary where, as here, petitioners were prevented from concluding a contract by the very fraud which is the subject of their federal securities law claim. *Cf. United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 868 (1975) (Brennan, Douglas & White, JJ., dissenting) ("Congress contemplated concurrent state and federal regulation in enacting the securities laws.").

For all of these reasons, Rule 10b-5 should apply to face-to-face negotiations for the purchase of a security regardless of whether a contract is formed. Accordingly, and contrary to the holdings of the courts below, petitioners are entitled as a matter of federal law to full consideration of their claim that they were defrauded by respondent SCM in the course of negotiations for the purchase of securities.[21]

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[20] Indeed, failure to extend standing to cover negotiations for the purchase of securities would be tantamount to saying that a negotiating party is free, under federal law, to commit any fraud it chooses during negotiations provided it breaks off negotiations at any time prior to entering into a contract.

[21] In particular, should this Court conclude that the courts below erred in denying standing, petitioners would argue on remand that respondent's fraudulent concealment of its intent to kill the deal amounted to a violation of Rule 10b-5.

II. THIS PETITION SHOULD BE GRANTED BECAUSE IT PRESENTS THE LOGICAL NEXT STEP AFTER *VISTA RESOURCES, INC. v. SEAGRAVE CORP.*

This Court recently granted the petition for certiorari filed in *Vista Resources, Inc. v. Seagrave Corp.*, 52 U.S.L.W. 3827 (U.S. May 14, 1984) (No. 83-1084). *Vista Resources* concerns the validity of the "sale of business" doctrine, under which some courts of appeals have held the federal securities laws inapplicable to sales of large blocks or all of the stock of a business.

The question presented in *Vista Resources* is whether a privately negotiated sale of the stock of a business is a transaction covered by the federal securities laws. This case raises a closely related issue: whether a defrauded party to such private negotiations must demonstrate the existence of a contract in order to sue under the anti-fraud provisions of the securities laws. Because of the close relationship between these issues, it may be desirable to grant the petition in this case and hear both issues on a consolidated or companion basis.

In any event, should the Court hold in *Vista Resources* that the anti-fraud provisions of the securities laws do apply to such transactions, this case provides the logical next step in the development of the law. The reasons why the sale of business doctrine should be rejected are the very reasons why standing should be found in this case, and turn on Congress' intent that a wide range of transactions involving purchases and sales of securities should be covered by the federal securities laws. *See* discussion *supra* at 15-16. Thus, at a minimum, in the event the Court decides not to grant this petition for certiorari at this time, it should hold this petition pending its ruling in *Vista Resources.*

CONCLUSION

Because this petition raises a recurring issue of considerable importance to the integrity of negotiations for the purchase or sale of securities, a writ of certiorari should issue to review the judgment of the Court of Appeals for the Second Circuit.

Respectfully submitted,

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